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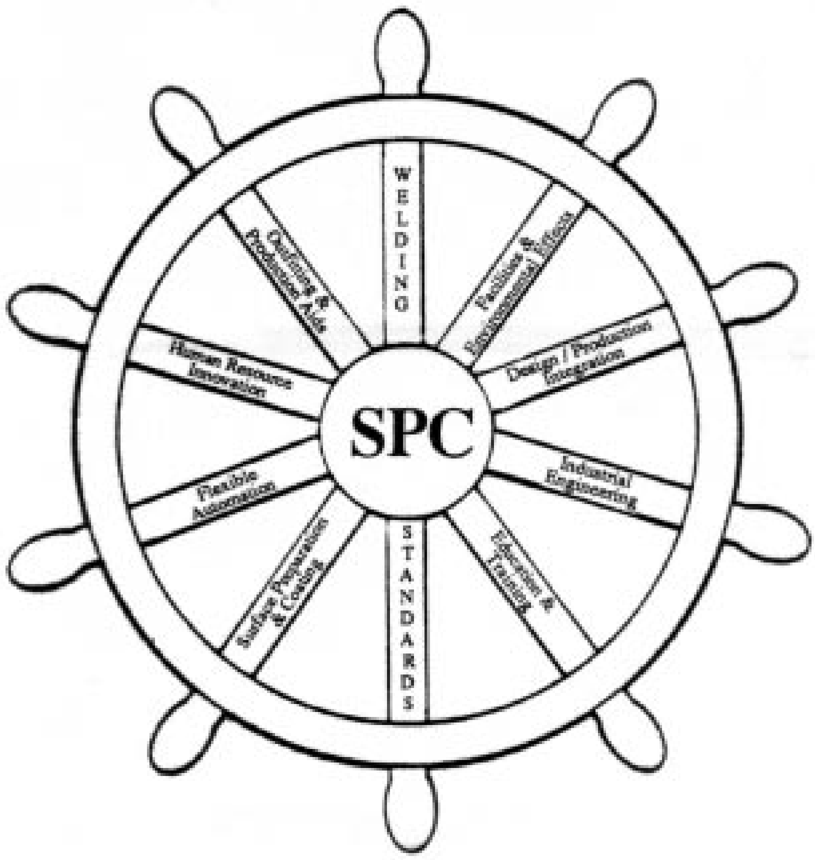

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In Search of a Level Playing Field: The Shipbuilders Council of America and the Issue of Foreign Shipbuilding Subsidies

8A-1

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ABSTRACT

This paper discusses the origins of decision by the Shipbuilders Council of America to file a petition under section 301 of the Trade Act of 1974 charging Japan, South Korea, West Germany and Norway with unfair trade practices in shipbuilding and ship repair. The progress of negotiations between the U.S. Trade Representative and foreign governments is presented as are the actions of the Organization for Economic Cooperation and Development (OECD) to address the reduction of unfair subsidies. The paper provides insight into the future course of action of the U.S. Government as well as the Shipbuilders Council of America in their continuing effort to provide for the reentry of U.S. shipbuilders into the worldwide commercial shipbuilding and ship repair markets.

BACKGROUND

During much of the 1980s, traditional shipyards throughout the world suffered from the worst shipbuilding recession in history, precipitated by the oil crisis of the mid-1970s and its subsequent detrimental effect on seaborne trade. Figure 1 shows the world shipbuilding orderbook in gross tons from 1970 to 1990.

The severity of the situation reflected not only the cyclical nature of the shipbuilding business responding to fluctuations in the shipping market, but also the massive overbuilding of shipbuilding capacity that had been undertaken in Japan and Europe in response to an unprecedented, highly-speculative demand for new ships--particularly tankers--during the 1960s and the early 1970s. During a ten-year period, for example, Europe increased its shipbuilding capacity by 136 percent and Japan by 650 percent. Exacerbating the situation was the entry into the marketplace of new, government-supported yards such as South Korea employing cheap labor.

The response of most governments of the world in the 1980s to this situation was to provide increased measures of shipbuilding assistance. If the success of these measures can be defined as keeping merchant shipbuilding capability alive, then these governments achieved some degree of success. Only three governments responded to the crisis by terminating commercial shipbuilding subsidies. The United States was first in 1981.

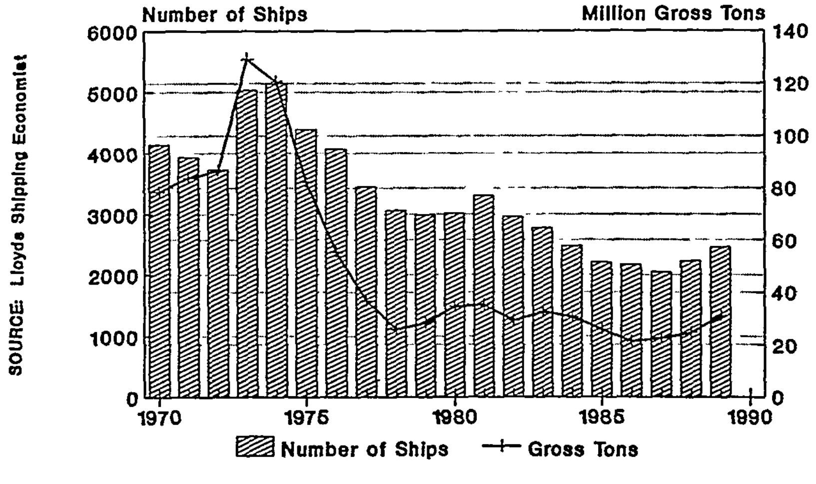

Figure 1. World Shipbuilding Orderbook.

followed later in the decade by Canada and Sweden. It is interesting to note that these three countries are also the only ones to suffer a complete collapse of commercial shipbuilding markets in the 1980s.

In the United States, all aid to domestic commercial shipbuilding, including the Construction-Differential Subsidy (CDS) program, was terminated. Forced to compete without government subsidies in a market dominated by government subsidies, American shipbuilders were unable to attract commercial customers. Until February 1990, when Matson Navigation ordered a containership from the San Diego-based National Steel and Shipbuilding Company (NASSCO). the last order for a large, oceangoing commercial ship placed with a U.S. yard was in 1984. Figure 2 shows the number of commercial ships on order at U.S. yards from 1970.

Lacking commercial customers, the U.S. shipbuilding industry turned to the U.S. Navy--and, to a lesser extent, the U.S. Coast Guard--for work in the 1980s. Government contracts alone, however, could not sustain the U.S. shipbuilding industrial base. The Shipbuilders Council of America (SCA) tracks shipyard closures from the baseline established by the Navy and the Maritime Administration's October 1982 Shipyard Mobilization Base of 110 shipyards, including both ship construction and ship repair facilities. By 1989, 46 shipyards had closed--a 42 percent decline--thereby putting the Shipyard Mobilization Base at 64 yards. Shipyard production worker employment in 1982 was 112,455. By 1989, that number had decreased to 76,282, representing a loss of 35,173 production workers, which is a 31 percent decline. Figure 3 shows the decline in the private U.S. shipyard base from 1982.

FACTORS IMPACTING SCA'S DECISION TO FILE PETITION

<u>Decline in Navy Work Forecasted</u>

During the early 1980s, the Navy's extensive rebuilding program sustained at least a portion of the nation's shipbuilding base, including those yards that normally would be considered commercial yards. Competition for Navy work was fierce, however, and, as the decade wore on, began to take its toll. At the same time, it was becoming clearer that the Navy workload would inevitably decline. Currently, the Shipbuilders Council predicts that the decline in FYs 1991 and 1992 will continue to be moderate, but that the remainder of the decade could well see

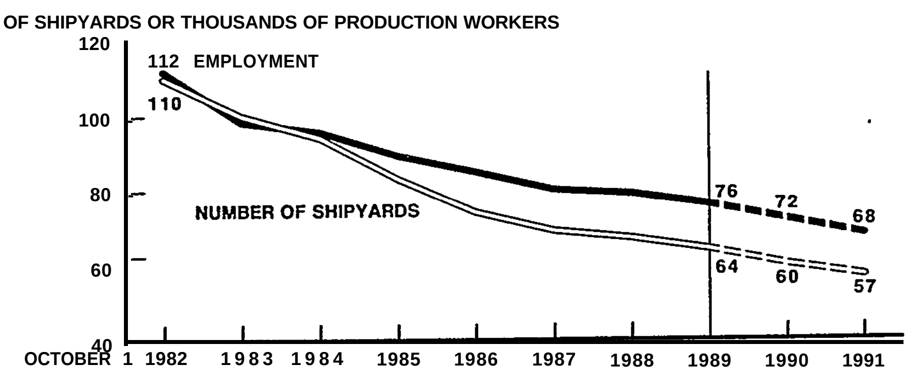

Figure 2. Private U.S. Shipyard Base.

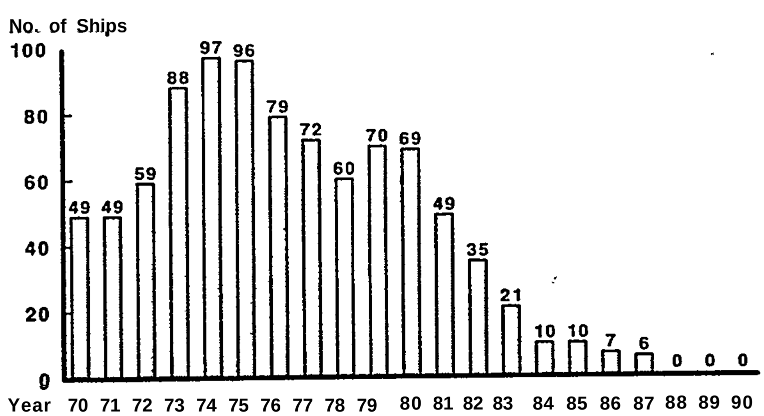

Figure 3. Commercial Ships on Order at U.S. Private Yards.

a much sharper decline, concomitant with decreases in the budget for naval ship construction. Consequently, U.S. shipbuilders cannot continue to count on Navy work.

Positive Changes in the Commercial Market

All of the shipbuilding forecasts during the past year and a half predict a significantly improved demand and increased prices for commercial ships in the 1990s. The primary reason for this optimism is the need for replacement ships. The world's merchant fleet is old: By 1992, more than 40 percent of the current fleet would be more than 20 years of age, and another 25 percent would be 15 to 19 years old.

Conditions in the commercial shipbuilding market are already improving. As of January 1, 1990, the number of commercial ships on order worldwide represented a 41 percent increase over the January 1, 1989 orderbook, and a 75 percent increase over two years ago. During the first quarter of 1990, there was even greater growth in the number of new ship orders. The shipyards of both Japan and South Korea have substantial backlogs. By the mid to late 1990s, deadweight tons (dwt) on order is expected to be at least double and as much as quadruple that of 1989.

Figure 4 shows the world orderbook for commercial ships to 1990 in millions of gross tons and a composite of orderbook forecasts from 1990 to 2000./1

Concurrent with the rise in new ship demand is the rise in ship prices. For example, five years ago, the average price of a medium-size very large crude carrier (VLCC) was around $44 million. Today, the price is more than double, and is still rising. Tight shipbuilding capacity is one important factor in continuing ship price escalation.

Subsidies Have Kent the U.S. out of Commercial Shipbuilding

With the anticipated decline in the Navy market, it is the commercial market that offers a long-term future for American yards. But the U.S. shipbuilding industry can only be a player in the international market if foreign shipbuilding subsidies are eliminated. The subsidization of commercial shipbuilding by foreign governments has effectively denied market access to American shipyards for nearly a decade. Not only have these subsidies been used to shore up shipbuilding industries and attract export customers, they have enabled the practice of producing ships at or below costs.

The impact of direct and indirect government subsidies on ship prices was summed up as follows by Drewry Shipbuilding Consultants in their November 1988 report, "World Market; Prospects to 2000":/2Shipbuilding

> "Directly, government assistance has led to reduced newbuilding prices by providing direct subsidies to individual

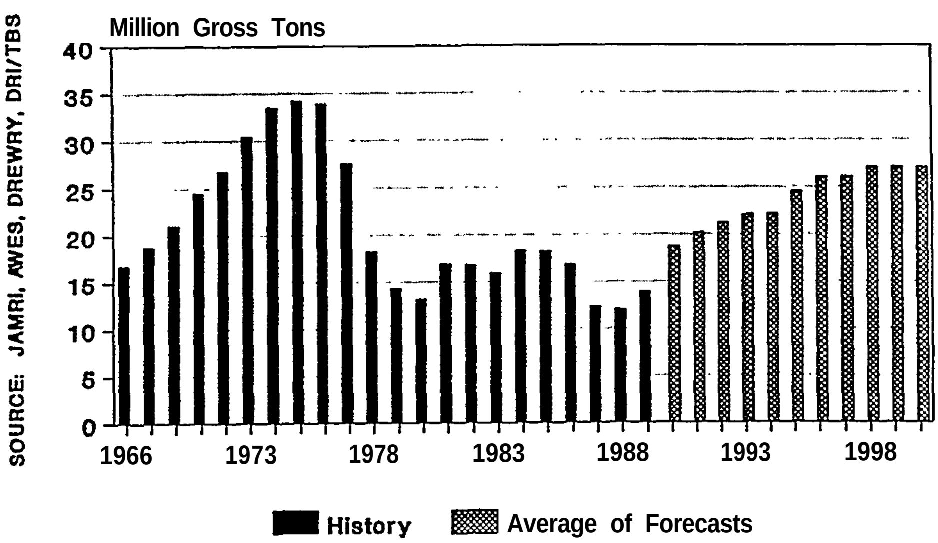

Figure 4. World Commercial Shipbuilding, History and Forecasts.

contracts and by providing an environment which allows yards to make available cheap finance. Indirectly, governments have allowed yards to run up substantial losses on newbuildings operations and have underwritten such losses."

In his presentation at the Shipbuilders Council of America's Marketing Seminar in January 1990/[3], Dr. Martin Stopford, Senior Shipping Economist at the Chase Manhattan Bank in London, explained that through subsidies governments prolonged shipbuilding overcapacity problems and depressed ship prices. He said that they did this partly for political reasons, partly in response to South Korea's shipbuilding expansion, and partly because they failed to understand the severity of the crisis. According to Dr. Stopford:

> "Instead of tackling the capacity reduction with a single clean cut, most shipbuilders tackled restructuring as a series of steps down, interspersed with periods of consolidation, during which each shipyard sought to maintain its market share at the expense of others by means of price cutting backed by subsidy."

At a conference in Genoa, Italy, in November 1989, Werner Fante, Director of the Association of West European Shipbuilders Association (AWES) also addressed the phenomenon of unprofitable pricing policies followed by shipbuilders during the 1980s:/[4]

> "Officially, it was pretended that low prices were based on high efficiency and losses were explained as the deplorable results of variations in exchange rates, higher material costs, and unforeseen burdens of ship financing. In a very few cases, the failure of wrong market strategies and fixing of prices without making provision for technical and commercial risks were admitted."

During this time, the U.S. Government unwittingly encouraged and supported shipbuilding subsidization by foreign governments in a variety of ways, while at the same time it demanded that U.S. shipbuilders "go it alone" in the international market. One of the U.S. Government's actions that was post damaging to American shipbuilders was the Section 615 amendment to the 1936 Merchant Marine Act. This special legislation allowed U.S.-flag operators receiving Operating-Differential Subsidy (ODS) payments from the U.S. government to buy from subsidized foreign yards during a temporary one-year "window" that subsequently was stretched to five years.

Of the 33 new ships built in foreign shipyards under the Section 615 amendment, all but three were built in the three countries that most heavily distorted the shipbuilding marketplace during the 1980s: South Korea, Japan, and West Germany. As one example, West German federal and regional governments contributed nearly $165 million to have two of its shipyards build five U.S.-flag containerships for American President Lines, which so far has received approximately $19 million from the U.S. Government to operate them. /5,6

Thus, the U.S. Government, through Section 615 legislation, encouraged one of its own subsidized industries to take advantage of a market distorted by the actions of foreign governments. It put our government in the position of rewarding the subsidy practices of our trading partners at the expense of our own country's shipbuilding industry.

Types of Subsidies

SCA's decision to file a Section 301 petition requesting the United States Trade Representative (USTR) to take action to terminate foreign shipbuilding subsidies followed its own preliminary investigation of the extent of these subsidies. The results of this investigation were published in October 1988 as a study of the subsidy programs of the then top-ten ship producing countries in the free world./7' The information contained in that study has subsequently been refined and expanded as more data has become available. In general, the major types of shipbuilding subsidies that have been and are still being provided are the following:

Special Financing (Credits). This category includes government-subsidies related to the financing of ship purchases for export or domestic customers and can include loans from government banks as well as interest subsidies and/or loan guarantees from federal and regional governments.

Construction Subsidy Grants. This type of subsidy encompasses direct government payments to shipyards for building ships, amounting to a certain percentage of the contract price. The Sixth Directive of the European Community, for example, specifically allows this type of subsidy and sets a limit on the percentage of the contract price that can be paid. This limit was 28 percent in 1988, 26 percent in 1989, and 20 percent in 1990. The limit, however, does not apply to contracts

with shipowners from those nations that are defined as less-developed countries (LDCs).

Shipyard Reorganization Aid. After a long period of hesitation, the EC and Japan finally began to recognize that they had overbuilt shipbuilding facilities in response to speculative ordering, and that they would have to take steps to reduce excess capacity. To ease the pain of restructuring, government-provided shipyard reorganization aid was instituted in Japan and the EC. This category covers a wide range of government subsidies to help shipyards modernize their facilities or to otherwise adjust to downsizing, and has included capital infusions, loan subsidies and guarantees, government buy-ups of redundant or outmoded facilities, and special tax benefits.

At times, the distinction has been blurred between reorganization aid for the purpose of shipyard rationalization and Shipyard Investment Aid--i.e., funding from governments to help shipyards build better shipbuilding plants and improve production techniques or to bail them out of financial difficulties.

Research and Development Aid. This type of aid involves government funding of research and development programs related to ship and/or ship production technology.

Tax Benefits. This category encompasses governmental tax measures to shipowners and/or shipbuilders that are not generally available to all other industries within that country. It includes tax reductions or tax exemptions to shipowners, such as special depreciation for ships and depreciation write-offs before the ship is delivered; and special tax provisions for shipyards, such as tax reductions on capital investments and exemptions from import taxes on materials.

The Omnibus Trade Act of 1988

In August 1988, awareness of the significant decline of the U.S. industrial base, coupled with the growing trade imbalance between the U.S. and its trading partners, precipitated stronger legislation to encourage foreign countries to accept American exports and to provide for retaliatory measures against countries that engage in unfair trade practices. Heartened by the legislation--which amends the 1974 Trade Act and was passed by overwhelming margins in both the House and the Senate--the Shipbuilders Council of America, as the trade association of the country's major shipbuilders, began to explore the options available to the U.S. shipbuilding industry under the new law.

Because the Tariff Schedules of the United States as well as judicial precedent have determined that ships are not "merchandise" or "articles" of import, it was concluded that Section 301, as strengthened in the Omnibus Trade Act of 1988 represented the most fruitful avenue for U.S. shipbuilders to pursue. Section 301 provides for U.S. Government action to respond to unfair trading practices. Among other things, the amendments of the 1988 Trade Act specified additional practices actionable under the Act, shortened the time limits for responding to a petition, transferred section 301 authority from the President to the United States Trade Representative (USTR), and provided a new mandatory retaliation requirement in cases involving violations of trade agreements or other "unjustifiable" practices.

The decision of the SCA to file a 301 petition was in line with the objectives of the Shipyard Recovery Program, the SCA-developed plan to restore the competitiveness of the U.S. shipbuilding industry in the commercial market. The Shipyard Recovery Program recognized that U.S. Government action to end worldwide shipbuilding subsidy practices was critical to dissolving the market distortions created by government subsidies.

THE 301 PETITION

Filing the Petition

The SCA hired the law firm of Collier, Shannon & Scott to prepare its Section 301 petition, which it filed with the Office of the U.S. Trade Representative on June 8, 1989./[8] The petition requested the USTR to take action to eliminate subsidies to foreign shipbuilding and repair industries and documented specific policies and practices of four countries. Under the terms of the Trade Act, the USTR had 45 days in which to weigh the petition's merits and to decide whether or not to initiate an investigation of the petition's allegations. The petition was examined by an interagency review group, comprised of representatives from various government agencies, including the Departments of State, Commerce, Justice, Transportation, Defense, Labor, Treasury, the Office of Management and Budget, the Council of Economic Advisers, and the U.S. Trade Representative.

Before and after filing the petition, the SCA worked to garner

political support for it on Capitol Hill. Ultimately, the petition received the support of 280 members of Congress --230 representatives and 50 senators--who signed letters urging the USTR to begin negotiations to eliminate foreign shipyard subsidies.

Countries Targeted in SCA Petition

The SCA's Section 301 Petition targeted the shipbuilding and repair subsidies in four countries: South Korea, Japan, West Germany, and Norway. Although all of the major shipbuilding nations engage in unfair subsidy practices, the Shipbuilders Council focused on these four because they have the most blatant subsidies which have caused the shipbuilding industry in the U.S. the most harm, and because together they accounted for over 55 percent of the world's commercial tonnage on order at the time of the filing. (At the end of 1989 the percentage had grown to 60 percent.) Table I compares the major kinds of shipbuilding aid programs in these countries against those of the United States. Table II shows the estimated amounts of shipbuilding aid budgeted in Japan and West Germany for 1987 and 1988, as compared with the United States. A narrative summary of the programs in each of the countries named in the petition, along with subsidy actions subsequent to the petition filing, follows:

South Korea. The South Korean government, largely through the state-owned Korea Development Bank, underwrote shipbuilding programs from their inception, allowing South Korea yards to pile up enormous debts while undercutting ship prices worldwide. At the time of the filing of SCA's petition, the debt of the four major South Korean

Table I
SHIPBUILDING AID IN 301-TARGETED NATIONS COMPARED WITH UNITED STATES

Countrv	Shipowner Special Financing.	Construction Subsidies	Yard Reorg. Aid; Investment Aid	Ship R&D Funding	Tax Benefits
JAPAN	Yes ***	unknown	Yes ***	Yes **	Yes
S.KOREA	Yes	unknown	Yes ***	unknown	Yes
WEST GERMANY	Yes	Yes ***	Yes ***	Yes	Yes
NORWAY	Yes ***	unknown	Yes	Yes	Yes
UNITED STATES	NO	NO	NO	Limited	Limited

Keyed where known: *** Very Significant, ** Significant, * Some

Table II
COMPARATIVE SHIPBUILDING SUBSIDIES BY COUNTRY
($ in Millions)

	UNITED STATES		W. GERMANY		JAPAN	
	1987	1988	1987	1988	1987	1988
Special Financing, Export Ships	0	0	197.6	139.8	138.3	210.6
Construction Subsidies	0	0	230.7	414.7	.1	0
Investment Aid	0	0	62.5	21.5	22.9	29.5
Restructuring Aid	0	0	7.0	106.1	562,6	4.1
Other Indirect Aid	1.4	.3	70.9	141.7	484.1	327.6
	$1.4	.3	8568.7	823.8	$1208.0	571.8

yards, equivalent to four times their equity capital, was $4 billion.

Subsequent to the petition filing, the South Korean government approved a rescue package for Daewoo and two other yards consisting of interest-free loans, debt moratoriums, tax exemptions, and other benefits, for Daewoo shipbuilders, the Korea Shipbuilding & Engineering Company (KSEC) and Inchon Shipbuilding Company. By far the biggest recipient of the government's largess was Daewoo. Repayment of Won250 billion ($372.7 million) of its Wonl.4 trillion ($2.1 billion) debt was put off for seven years, and the yard was given a new loan of Won150 billion ($223.6 million). The South Korean government also has ship finance programs.

Japan. Since 1978, the Japanese government has helped its shipbuilders to reduce their massive overcapacity, the buildup of which the government had encouraged in the first place. In return for a commitment by the industry to down- size, the government allowed the industry to form a cartel and provided financial aid and loan guarantees associated with the mothballing of facilities, as well as other subsidies, which allowed the yards to operate in the red for a number of years. Now that the market has vastly improved, shipbuilders are modernizing and reopening their mothballed facilities.

The Japanese government has always been heavily involved in ship and shipbuilding-related research and development. In JFY 1989 the Government adopted a new program described by the Director-General of the Maritime Technology and Safety Bureau, Ministry of Transport (MOT), as "a system to encourage technical development efforts to materialize such sophisticated ships which could well meet the needs of the next generation."/9 Projects include development of 3 five-year fast cargo ship project called Techo-Superliner 93 and a high reliability diesel engine for ships.

The Japanese government also provides partial funding for export ships through the Export-Import Bank, and for domestic ships (particularly high-technology ships) through the Japan Development Bank. Regarding domestic ship financing, subsequent to the SCA's 301 filing, the MOT announced that its JFY 1990 budget request was Yen66.4 billion (about $458 million), which was considerably higher than the JFY 1989 budget./1O

West Germanv. Both federal and regional governments subsidize commercial shipbuilding in West Germany through direct cash infusions, ship production grants, preferential financing, and credit guarantees. On the federal level, money for shipbuilding subsidies has been paid out of budgets for defense and for economic assistance to developing countries, as well as from funds for direct shipbuilding assistance. Regarding the latter, subsequent to SCA's filing of the 301 petition, the German government announced that it would add Dm300 million ($101.7) more to its ship production aid program for FY 1990, bringing this year's allotment to Dm343 million ($174.4 million)./11

Two shipbuilding groups have particularly benefitted from government subsidies: state-owned Howaldtswerke Deutsche-Werft (HDW) and partially government-owned Bremer Vulkan. Most of the ships on order at the HDW yard in 1987, 1988, and 1989 received some government subsidy, with the level of aid particularly high in 1987 and 1988. Two of the contracts were especially controversial, although they ultimately received approval from the EC Commission: the previously-mentioned American President Lines (APL) containership deal and Zim Israel containership deal. Of the subsidies paid for the APL ships (three built at HDW and two at Bremer Vulkan), Dm125 million ($69.4 million) came out of funds from the German Ministry of Defense despite the fact that the vessels are merchant ships and cannot contribute to the NATO sealift pool since they are operating in the Pacific and cannot transit the Panama Canal. The U.S. Government contributed to this process by waiving research and development costs on the German purchase of HARPOON.

In the Zim Israel case, the West German government termed Israel a "lesser-developed country" so that it could bypass EC rules and pay a 25.4 percent on an estimated $100 million contract to build four containerships. (Originally, two of the ships were to be built at the Bremer Vulkan yard, but the entire order was transferred to HDW.) In 1989, the German government provided Zim Israel with another low-credit package and a 30 percent subsidy so that HDW could build three more ships.

Information on German R&D programs has been difficult to come by. It was not known until after the filing of the 301 petition, for example, that the Federal Ministry of Research and Technology (BMFT) and the Federal Ministry of Economics are subsidizing R&D in computer-controlled ship production techniques.

NorwaY. The government of Norway

provides domestic and foreign shipowners with a variety of attractive financing programs for the purchase of ships, fishing vessels, and equipment. One program, for example, offers interest rates as low as two percent. Another program makes loans available at four percent, with 12 years to repay, including a three-year grace period.

THE GOVERNMENT'S RESPONSE

USTR's Request to Withdraw Petition

On July 21, 1989, the Shipbuilders Council of America and the United States Trade Representative announced that they had reached an agreement: The SCA would withdraw its petition temporarily to allow the USTR a period of time in which to pursue the termination of shipbuilding subsidies through traditional negotiating channels before using the more confrontational remedies provided under Section 301 of the Trade Act.

In a formal statement, USTR Carla Hills acknowledged that foreign government subsidization of ship construction and repair was a "serious problem." She announced that the countries named in, SCA's 301 petition had declared their willingness to negotiate [with West Germany represented only through the European Community (EC)], and that she intended to engage in talks with these countries, primarily through the mechanisms of the Organization for Economic Cooperation and Development (OECD) and the Uruguay Round of the General Agreement on Tariffs and Trade (GATT). Ambassador Hills promised that if insufficient progress was not made in these negotiations by March 31, 1990, then the SCA would be invited to resubmit its petition.

N e g o t i a t i o n s six

Immediately after the agreement was reached between the USTR and the SCA, a U.S. Trade Policy Review Group (TPRG) began devising a strategy for negotiating a multilateral agreement to discipline shipbuilding subsidies. The U.S. State Department had already talked with officials at the OECD's shipbuilding group, Working Party Six, and had applied for full membership in June 1989, thus paving the way to use that body as a forum for subsidy talks. (Other members of Working Party Six are Japan, Germany, Norway, Finland, Great Britain, France, Ireland, Denmark, the Netherlands, Sweden, Belgium, Italy, and Spain. South Korea, which is not an OECD member, is represented through a special liaison group.) In addition, Working Party Six already had on the books an agreement to remove shipbuilding subsidies that could be used as a framework.

The RGA. The "Revised General Arrangement (RGA) for the Progressive Removal of Obstacles to Normal Competitive Conditions in the Shipbuilding Industry," was adopted by the OECD Council on Feb. 23, 1983. Signed by 14 nations plus an EC representative, the RGA committed the signatories to refrain from increasing aid or adding new shipbuilding subsidies, and to gradually eliminate existing subsidies. That commitment, however, was largely ignored. In general, shipbuilding aid in the countries participating in the agreement was not reduced; moreover, in many of the countries, the level of aid was increased and new shipbuilding subsidy programs instituted.

Among the "obstacles to normal competitive conditions in the shipbuilding industry" the RGA signatories pledged to reduce were:

a) Government-subsidized export credits;
b) Direct subsidies to the shipbuilding industry;
c) Customs tariffs or any other import barrier;
d) Discriminatory tax policies;
e) Discriminatory official regulations or internal practices;
f) Specific aid for investments;
g) Subsidies for restructuring of the domestic shipbuilding industry;
h) All other forms of indirect public aid which are obstacles to normal competitive conditions in the shipbuilding industry.

The U.S. Proposal. On October 16, 1989, the U.S. delegation brought to the Working Party Six negotiating table its proposal to accelerate implementation of the RGA. Under the terms of the proposed agreement, participating governments would be required to refrain immediately from implementing new or increased measures of shipbuilding assistance and to develop individual timetables for eliminating existing shipbuilding subsidies, with final termination by the end of 1991. The proposal included a provision calling for the development of a mechanism to enforce the agreement.

The U.S. proposal also attempted to more clearly define the types of shipbuilding subsidies encompassed by the general categories stated in the RGA. Tied aid (mixed foreign aid and supplier credits used to sell ships to developing countries) and government ownership of merchant shipyards were added to the list of market distorting practices to be eliminated.

Although there were objections to

different parts of the U.S. proposal from the individual member-nations of Working Party Six, the overall response was to "agree in principle" to eliminate shipbuilding subsidies and to continue negotiations. Various drafts of proposals and counter-proposals were presented over the next five months. The U.S. negotiating team eliminated tied aid from its proposal and added language to exempt purely domestic programs from the scope of measures of assistance to be eliminated. Tied aid was to be taken up in other negotiations involving the U.S. Treasury Department.

PROGRESS TO DATE

The Current Draft Document

General Description. As of this writing, the format of the draft document consists of the subsidy convention--which basically describes the purpose and scope of the agreement. More importantly, it establishes mechanisms to monitor, verify, and enforce the provisions of the agreement. Annex I identifies the subsidies to be prohibited. Annex 2 sets the timetable for implementation of the agreement, and Annex 3 contains 3 list of programs that would be exempted from coverage under the subsidy convention. Each country has proposed a program that would be included in Annex III, which at the time of this writing had not yet been prepared.

Annex I. The following are the types of shipbuilding and repair subsidies that are under negotiation for termination (keep in mind that the preparation date of this paper is considerably earlier than the date of its presentation, and that the draft agreement may have changed by August):

a) Officially-supported export credits at terms more favorable than those of the OECD Understanding on Export Credits for Ships; i.e., 80 percent loans over 8½ years at 8 percent interest. In other words, this subsidy will continue as currently allowed. However, it appears that sometime in the future ship export credits will be shifted out of Working Party Six and into the OECD's Export Credit group. When that happens, ships will be subject to the same export credit provisions allowed within the OECD for other industries; namely. government-supported financing at the commercial interest reference rate (CIRR) in each country.

b) Direct official support for the operations of the commercial shipbuilding and repair industry, such as grants, below-market loans and loan guarantees, debt forgiveness, equity infusions, and the provision of other preferential goods and services.

c) Direct official support for investment in the commercial shipbuilding and repair industry, including the categories of aid mentioned above under operational aid, plus aid for research and development and restructuring Support. What constitutes acceptable R&D support is still under negotiation. Acceptable restructuring support would include measures tied to permanent closings of shipbuilding capacity and/or aid linked to the social effects of closures, such as problems associated with worker displacements.

d) Customs tariffs. This item is still under negotiation.

e) Tax policies and practices favoring the shipbuilding and repair industry. Exceptions still need to be spelled out.

f) Official regulations and practices and import barriers other than tariffs for new-built ships. The scope of this item still has to be determined.

g) Other forms of indirect support to yard activities. Agreement on the scope of this item has not yet been reached.

h) Publicly-owned shipyards. The survival of this item as a prohibited measure is doubtful, although the U.S., Japan and South Korea are pushing the EEC to adopt the provision.

j) Private practices. This item is under negotiation.

The European Commission, which is negotiating on behalf of the member nations of the European Community, has introduced an anti-dumping proposal which, when and if it is accepted, probably would be incorporated into this annex. The purpose of the proposal is to discourage builders from selling ships at "unfair" prices; meaning prices insufficient to cover the full cost of production plus a reasonable margin of profit. The U.S. endorses such a proposal.

Annex II, This section deals with the time period for phasing out the shipbuilding subsidies proscribed in Annex I. Current proposals range from immediate to five full years for ter-

mination of some measures of government support. The U.S. proposal says that it would require two years to repeal whatever statutes are on U.S. books that relate to shipbuilding support.

Missed Deadlines. The U.S. negotiating team pressed for a signed document by March 31, 1990, the deadline promised U.S. shipbuilders by USTR Carla Hills. When the date was not met, the SCA expressed "extreme disappointment" that the signatory nations had not been able to agree on a text outlining the practices to be outlawed and the details of the mechanism by which the countries would monitor, verify, and enforce the agreement.

Nevertheless, SCA felt that significant progress had been achieved, and, in consultation with the USTR, decided to defer refiling a 301 petition in order to allow the Administration more time. The SCA was hopeful that an agreement would be achieved by May 31, 1990, in time for the OECD Ministerial Conference, as was originally intended when the negotiating schedule was set in the summer of 1989. However, this was not to be. The U.S. trade negotiators returned from the May 5 and 6 OECD Working Party No. Six meeting in Paris without a signed agreement and extremely frustrated by their lack of success. Interestingly, the fact that subsidies for American shipbuilders were cut off over eight years ago has made the position of the U.S. negotiators more difficult. They have very little leverage in the talks because the unsubsidized U.S. shipbuilding industry has nothing of trade-off value to give up.

WHAT'S NEXT?

At this point, the U.S. team is prepared to keep on with the negotiations. The team feels that enough progress has been made to allow the process to continue. The next negotiations among the full working party are scheduled for June 18, 1990. Among the issues that need to be ironed out: the subsidy definitions in Annex 1 still need clarification; the minimum vessel size to which the subsidy prohibitions apply; what current programs will be exempt from the agreement (grandfathered); the time frame for the subsidies' phaseout; and how to set up the remedy process.

The SCA's concern is that the negotiations could continue to drag on interminably. Time is of the essence to U.S. shipbuilders, since they will continue to be denied access to the commercial market as long as foreign shipbuilding subsidies remain in place. The tenacity of the U.S. trade team might indeed result in an eventual victory, but it will be a hollow victory if it comes too late for U.S. yards.

It is already clear that the goal of the U.S. proposal to have all shipbuilding subsidies terminated by the end of 1991 will not be accomplished. If there is no resolution of the outstanding issues during the June Working Party Six meetings, then the negotiations are likely to slow down until the spring of 1991, since by fall the U.S. trade team will be heavily involved in the concluding sessions of the Uruguay Round of GATT (General Agreement on Tariffs and Trade) negotiations.

Even under the most optimistic scenario, which assumes that agreement is reached between the parties at the June Working Party Six meetings, shipbuilding aid could not be eliminated until the end of 1992. This means that for at least the next two years, the U.S. industry-- as the only unsubsidized shipbuilders in 'the world actively represented in Working Party Six--will not be able to benefit from the commercial shipbuilding boom of the 1990s as the subsidized shipyards of the world consolidate their market position.

An option currently under consideration by the SCA is to refile its 301 trade complaint, perhaps widening the scope of the petition to include those countries within the EEC that have been the most obstructionist in the negotiations. But whether remedies are pursued under Section 301 of the U.S. Trade Act, through the OECD, or through some other mechanism, it is clear that effective action can only come from the government level. In the last analysis, the achievement of a level playing field--and the survival of the U.S. shipbuilding industry--will depend on the willingness of the U.S. government to do whatever it takes to get foreign governments to stop the practices that are distorting the international shipbuilding market and to do it before market demand disappears.

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